

MINUTES OF MEETINGS
of the
FEDERAL ADVISORY COUNCIL

October 6-7, 1946

December 1-2-3, 1946

and of the

MEETING

of the

EXECUTIVE COMMITTEE

November 6, 1946

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

October 6, 1946

The third statutory meeting of the Federal Advisory Council for 1946 was convened in Room 336 of the Mayflower Hotel, Washington, D.C., on Sunday, October 6, 1946, at 2:05 P.M., the President, Mr. Brown, in the Chair.

Present:

Mr. Charles E. Spencer, Jr.	District No. 1
Mr. John C. Traphagen	District No. 2
Mr. David E. Williams	District No. 3
Mr. John H. McCoy	District No. 4
Mr. A. L. M. Wiggins	District No. 5
Mr. J. T. Brown	District No. 6
Mr. Edward E. Brown	District No. 7
Mr. James H. Penick	District No. 8
Mr. Julian B. Baird	District No. 9
Mr. A. E. Bradshaw	District No. 10
Mr. Reno Odlin	District No. 12
Mr. Herbert V. Prochnow	Acting Secretary

Absent:

Mr. Ed H. Winton	District No. 11
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On motion, duly made and seconded, the Acting Secretary's notes and the printed minutes of the meetings of the Council on February 17-18, 1946, and on May 19-20, 1946 and the meetings of the Executive Committee of the Council on April 24, 1946 and June 26, 1946, copies of which had been sent previously to the members, were approved.

On motion, duly made and seconded, the following resolution was unanimously adopted:

FEDERAL ADVISORY COUNCIL

**RESOLUTION UNANIMOUSLY ADOPTED BY
THE FEDERAL ADVISORY COUNCIL IN SESSION
WASHINGTON, D. C., OCTOBER 6, 1946**

THE MEMBERS OF THE FEDERAL ADVISORY COUNCIL DESIRE TO EXPRESS BY MEANS OF THESE RESOLUTIONS THEIR PROFOUND SENSE OF LOSS ON THE OCCASION OF THE DEATH, ON AUGUST 8, 1946, OF THEIR FELLOW-MEMBER, ROBERT STRICKLAND.

MR. STRICKLAND NOT ONLY SERVED HIS BANK AND THE BANKING PROFESSION WITH DISTINCTION FOR MANY YEARS, BUT IN ADDITION SERVED WITH EQUAL FIDELITY NUMEROUS CULTURAL, EDUCATIONAL AND BUSINESS INSTITUTIONS, GIVING GENEROUSLY OF HIS ADVICE AND COUNSEL.

MR. STRICKLAND HAD THE AFFECTION AND HIGH REGARD OF ALL THE MEMBERS OF THIS COUNCIL WHO SERVED WITH HIM.

RESOLVED, THAT THIS RESOLUTION BE SPREAD UPON THE BOOKS OF THE COUNCIL, AND THAT A COPY THEREOF BE SENT TO MR. STRICKLAND'S FAMILY AS AN EXPRESSION OF THE HEARTFELT SYMPATHY OF THE FEDERAL ADVISORY COUNCIL.

The Council considered at length the proposed amendments (H.R. 7211 and S.2494) concerning the F. D. I. C. It was unanimously agreed the Council should take no action now on these amendments.

There was a brief discussion regarding the mechanics of Reserve bank buying of Treasury bills. It was concluded that in the absence of a plan better than the present arrangement, no action should be taken.

The question of the modification of Regulation W was considered at length, and it was agreed the Council would advise the Board of Governors that the Council believes controls should be eliminated as goods come into the market in adequate supply, and that the controls should be eliminated now on all but a few items. The Council does not believe that Regulation W should become a permanent part of the economy of the nation.

The Council also discussed the present status of the government bond market, the debt retirement and refunding program of the Treasury and the question of whether it is desirable to make recommendations to Congress for changes in banking laws by means of a special report embodying the joint recommendations of the Board of Governors of the Federal Reserve System, the presidents of the Federal Reserve banks and the Federal Advisory Council as was done in January, 1941, rather than confining these recommendations to the Annual Report of the Board of Governors of the Federal Reserve System.

The Council also considered whether it would be desirable that some plan be developed with the RFC whereby the holdings of the RFC of preferred stock or capital debentures in banks could be transferred to local ownership.

There was some discussion regarding the 100 per cent margin requirements. The Council agreed as to the advisability of changing the present requirements in connection with persons who wish to borrow on stocks to exercise rights.

The meeting adjourned 5:38 P.M.

HERBERT V. PROCHNOW
Acting Secretary.

MINUTES OF JOINT CONFERENCE OF THE FEDERAL ADVISORY COUNCIL
AND THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

October 7, 1946

At 10:43 A.M., a joint conference of the Federal Advisory Council and the Board of Governors of the Federal Reserve System was held in the Board Room of the Federal Reserve Building, Washington, D.C.

Present: Members of the Board of Governors of the Federal Reserve System: Chairman Marriner S. Eccles; Vice Chairman Ronald Ransom; Governors Ernest G. Draper, R. M. Evans and James K. Vardaman, Jr.; also Messrs. Elliott Thurston, Assistant to the Chairman; Chester Morrill, Special Adviser to the Board of Governors; Leo H. Paulger, Special Adviser to the Board of Governors; S. R. Carpenter, Secretary of the Board of Governors; Merritt Sherman, Assistant Secretary of the Board of Governors; George B. Vest, General Counsel; Woodlief Thomas, Director, Division of Research and Statistics; Robert F. Leonard, Director, Division of Examinations; Edward L. Smead, Director, Division of Bank Operations; and Carl E. Parry, Director, Division of Security Loans.

Present: Members of the Federal Advisory Council: Mr. Edward E. Brown, President; Mr. Charles E. Spencer, Jr., Vice President; Messrs. John C. Traphagen, David E. Williams, John H. McCoy, A. L. M. Wiggins, J. T. Brown, James H. Penick, Julian B. Baird, A. E. Bradshaw, Reno Odlin and Herbert V. Prochnow, Acting Secretary.

Absent: Mr. Ed H. Winton.

A brief discussion took place regarding the proposed amendments (H.R. 7211 and S. 2494) concerning the F.D.I.C. Chairman Eccles indicated the Board of Governors had taken no definite action regarding the proposed amendments.

Chairman Eccles advised the Council that the subject of Reserve bank buying of Treasury bills is still under study by the Board of Governors.

The members of the Council and the Board of Governors discussed at some length the present status of the government bond market and plans the government may have regarding the debt and maturing obligations.

The President of the Council informed the Board of Governors that the Council believes Regulation W should be modified to eliminate many items from control. President Brown stated that the Council understood some months ago that the restrictions would gradually be released and finally be eliminated as goods came into the market in adequate supply.

A brief discussion took place regarding the question of the preferred stock and capital debentures of banks now held by the RFC.

The Council and the Board then discussed the 100 per cent margin requirements for purchasing listed securities. The President of the Council informed the Board that the Council believes something should be done now to enable owners of stocks to borrow for the purpose of exercising rights.

Chairman Eccles reported that the Board of Governors had not discussed further the Revised Bank Holding Company Bill.

The meeting adjourned at 1:20 P.M.

HERBERT V. PROCHNOW
Acting Secretary.

MINUTES OF MEETING OF THE FEDERAL ADVISORY COUNCIL

October 7, 1946

At 2:10 P.M., the Federal Advisory Council reconvened in the Board Room of the Federal Reserve Building, Washington, D.C., the President, Mr. Brown, in the Chair.

Present: Mr. Edward E. Brown, President; Mr. Charles E. Spencer, Jr., Vice President; Messrs. John C. Traphagen, David E. Williams, John H. McCoy, A. L. M. Wiggins, J. T. Brown, James H. Penick, Julian B. Baird, A. E. Bradshaw, Reno Odlin and Herbert V. Prochnow, Acting Secretary.

Absent: Mr. Ed H. Winton.

Dr. Woodlief Thomas, Director, Division of Research and Statistics, discussed "Latin American Trends."

The meeting adjourned at 3:22 P.M.

HERBERT V. PROCHNOW
Acting Secretary.

NOTE: This transcript of the Acting Secretary's notes is not to be regarded as complete or necessarily entirely accurate. The transcript should be considered as being strictly for the sole use of the members of the Federal Advisory Council.

H. V. P.

The Acting Secretary's notes on the meeting of the Federal Advisory Council on October 6, 1946, at 2:05 P. M., in Room 336 of the Mayflower Hotel, Washington, D. C.

All members of the Federal Advisory Council were present except Mr. Ed H. Winton.

The Acting Secretary's notes and the printed minutes of the meetings of the Federal Advisory Council of February 17-18, 1946, and May 19-20, 1946, and of the Executive Committee for April 24, 1946, and June 26, 1946, copies of which had been previously sent to members of the Council, were approved.

The Council adopted the following resolution:

Resolution unanimously adopted by the
Federal Advisory Council in session
Washington, D. C., October 6, 1946.

"The members of the Federal Advisory Council desire to express by means of these resolutions their profound sense of loss on the occasion of the death, on August 8, 1946, of their fellow-member, Robert Strickland.

"Mr. Strickland not only served his bank and the banking profession with distinction for many years, but in addition served with equal fidelity numerous cultural, educational and business institutions, giving generously of his advice and counsel.

"Mr. Strickland had the affection and high regard of all the members of this Council who served with him.

"Resolved, that this resolution be spread upon the books of the Council, and that a copy thereof be sent to Mr. Strickland's family as an expression of the heartfelt sympathy of the Federal Advisory Council."

PROPOSED AMENDMENTS CONCERNING THE F.D.I.C. (H.R.-7211 and S.2494)

E. E. BROWN states that the proposed amendments authorize the Corporation to retire outstanding capital stock provided that no retirement of stock results in the net worth of the Federal Deposit Insurance Corporation being less than \$1 billion. The amendments also provide that each appointive member, of whom the Chairman of the Corporation is one, shall hold office for six years and shall receive compensation at the same rate as that prescribed for the members of the Board of Governors of the Federal Reserve System, together with travelling expenses. Brown asks Williams to comment on these amendments inasmuch as this item on the agenda was originally suggested by Mr. William Fulton Kurtz.

WILLIAMS states he has nothing in particular to suggest but that Kurtz has indicated the President of the Council is thoroughly familiar with the matter.

WIGGINS thinks that the Council should perhaps discuss the matter but not pass any resolution regarding it. Many bankers have believed that the government should not participate in the affairs of private enterprise, and some of these bankers think that if they are to be consistent they should advocate the return of the government capital in this instance. Wiggins does not believe that the situation is necessarily comparable. He does not believe either that anyone knows how much is required to make the fund adequate. Many people believe that the United States government is guaranteeing deposits. Crowley was opposed to any change in the basis of assessment. Wiggins believes it might be desirable to return what the Treasury put into the fund.

E. E. BROWN reports that he attended several meetings of bankers who discussed this subject. He states that Harl originally had favored the plan of keeping the fund at \$1 billion with fluctuating assessments. The fund would be a mutual idea. At these meetings there was some feeling that if the government money was returned to the Treasury and the other funds to the Federal Reserve banks some persons who now think it is a government guarantee might feel the government had withdrawn its guarantee. Harl's idea of fluctuating assessments might lead to the elimination of assessments in good times and result in heavy assessments in periods of depression. The return of the money to the Federal Reserve banks might lead these banks to use the funds for small loans or for some other purpose. Brown is inclined to believe that a number of bankers would favor leaving the situation alone and not making any change at the present time.

WIGGINS reports that the bankers originally opposed a flexible assessment arrangement, and he believes the bankers should stand by that viewpoint now.

E. E. BROWN thinks that if the bankers support this bill it may lead to the advancement of the flexible assessment idea.

SPENCER says that the National Association of Bank Auditors and Comptrollers has recently made a number of suggestions on the subject.

E. E. BROWN understands that these suggestions will go out as a questionnaire to be answered by the policy-making officials in each bank.

WIGGINS believes that the bankers should proceed with care on this subject because of the danger of undesirable proposals that may develop later on.

E. E. BROWN thinks that Eccles may favor any proposal which would return money to the Federal Reserve banks which might be used by them for small loans or other purposes.

WIGGINS suggests saying to the Board that the Council discussed the matter but deferred action.

E. E. BROWN. All members of the Council are apparently in agreement with the viewpoint that no action should be taken on these amendments now. The proposal is comparable to opening Pandora's box. No one knows what will come out when the box is opened. Brown states he will inform the Board that the Council has deferred action at least until the new Congress meets.

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AT PRESENT THE FEDERAL RESERVE BANKS BUY TREASURY BILLS IN THE OPEN MARKET THROUGH BROKERS. THIS IS A SOMEWHAT FICTITIOUS TRANSACTION BECAUSE ACTUALLY THERE ARE NO OTHER BIDDERS FOR MOST OF THE BILLS BOUGHT. IT HAS BEEN SUGGESTED THAT THE FEDERAL RESERVE BANKS, UNDER AN ARRANGEMENT WITH THE TREASURY, CONVERT THEIR BILL HOLDINGS INTO A SINGLE PIECE OF PAPER THAT WOULD NOT REQUIRE WEEKLY BUYING AND LIQUIDATION. HOWEVER, THIS MIGHT BE CONSTRUED AS DIRECT BORROWING BY THE TREASURY FROM THE FEDERAL RESERVE BANKS. IT SEEMS DESIRABLE THAT THE MECHANICS OF RESERVE BANK BUYING OF TREASURY BILLS SHOULD BE REVISED. THE QUESTION IS WHAT IS THE BEST PLAN TO USE.

E. E. BROWN asks Wiggins to comment on this subject.

WIGGINS believes that sooner or later some legislation will be introduced to cover this matter. He does not know what is the real answer to this problem.

TRAPHAGEN thinks some advantages do accrue to banks inasmuch as they are able to keep their funds employed.

E. E. BROWN states the present device is a fictitious one, but it at least keeps the fiction of not borrowing directly from the Treasury. The worst inflation periods in history have developed when the Treasuries of nations borrowed directly from their central banks.

TRAPHAGEN prefers to see the situation remain as it is rather than to have direct borrowing from the Federal Reserve banks by the Treasury.

ODLIN believes it is far better to leave the matter as it is even if the transaction is somewhat fictitious.

WIGGINS favors the present arrangement even if it is fictitious, as it is better than direct borrowing by the Treasury from the Federal Reserve banks.

E. E. BROWN states that the dealers make practically nothing out of the transaction and that the income hardly covers the handling costs.

ODLIN believes that if the Treasury resorted to direct financing of its bills, it might open the door still further to direct financing with the Federal Reserve banks.

WIGGINS thinks that in the absence of a plan better than the present arrangement, action should be deferred now.

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THE PRESENT STATUS OF THE GOVERNMENT BOND MARKET AND PLANS WHICH THE TREASURY MAY HAVE WITH RESPECT TO THE CONTINUATION OF DEBT RETIREMENT AND REFUNDING OF MATURING OBLIGATIONS.

E. E. BROWN asks Traphagen to comment on this topic.

TRAPHAGEN believes that debt retirement has apparently gone almost as far as the Treasury had originally planned. He asks whether it would not be desirable to inquire of the Board what the plans are for the future.

E. E. BROWN. The Board may decline to discuss the matter as the members of the Board may not themselves have plans for the future handling of the debt. He believes the Treasury may keep the 7/8 per cent certificates at par. In the last ninety days there has been a material change in the situation. It has been a question of keeping the 2-1/2's from going down instead of going up.

E. E. BROWN believes the 2-1/2's of 67-72 should be kept at slightly above par, say at 100-1/2. Burgess thinks 101 is the desirable figure. If the 7/8 per cent certificates are not kept at par, they may go to one per cent. There is an opportunity now to buy railroad securities at a satisfactory rate if the government does not wish to put out a three or four year security at 1-1/2 per cent. Brown believes that Snyder may be willing to have the Treasury balances decline to \$3 to \$5 billion. If the government should refund the 1-1/2's into 7/8 per cent certificates, the 7/8 per cent certificates will go to the Treasury. Savings banks can now buy corporate obligations that have satisfactory yields.

WILLIAMS thinks the Council might ask the Board what its plans are.

E. E. BROWN believes the Treasury likes to feel comfortable with its balances, whereas the Board favors smaller balances. Brown will ask the Board for any information they wish to give regarding future plans concerning the debt.

WIGGINS asks why it is necessary to support the 7/8 per cent rate. He states that perhaps they should recognize the present natural trend in rates.

SPENCER asks Wiggins what he thinks the rate would be if the Board and the Treasury did not hold it at 7/8 per cent.

WIGGINS thinks it might be one per cent.

TRAPHAGEN states the Board and Treasury might then have trouble supporting the long-time rate.

E. E. BROWN reports that the feeling is strong in the Treasury that the 7/8 per cent rate on certificates must be maintained.

WIGGINS believes the effect of maintaining an artificial rate situation is that government securities will move out of the banks into the Federal Reserve System.

BAIRD thinks that the differential between commercial loan rates and rates on government obligations will lead the banks to move their governments and that the government obligations will go into the Federal Reserve System.

E. E. BROWN. There is probably not a great deal of difference between a situation where the Federal Reserve banks hold the government debt and one where the commercial banks hold the government debt.

TRAPHAGEN does not believe anything will be done to increase the cost of carrying the government debt.

PENICK asks what the results were when representatives of the insurance companies and savings banks met with the Treasury recently.

SPENCER understands that the Treasury asked the insurance companies where they would obtain the funds to buy the obligations which they thought should be issued.

WIGGINS. If the government issued a 2-1/2 per cent bond, the government might find that insurance companies and others would buy these obligations and unload other government obligations. Consequently, the government is not likely to act until it knows how to close that door.

E. E. BROWN reports that the whole demand for money has changed in the larger cities. Three factors are causing a relatively heavy demand for money at least in the larger centers: (1) A higher price level which results in a greater cost for inventories and in larger receivables; (2) increasing inventories due to strikes, partially manufactured goods, freight embargoes, car shortages, and O. P. A. regulations; and (3) companies with expansion programs had expected to finance these programs by selling stock, but the stock market decline has made it necessary for these companies to go to banks for loans. Money is tighter now than it has been for several years.

WIGGINS asks to what section of the country the deposits are now being shifted.

PENICK believes they will go largely to the country banks, but he also believes that later, when tractors, automobiles and other goods are available, the deposits may move to the centers in which these goods are manufactured.

E. E. BROWN cites cases of loans to those in the rice, bean, and soybean industries where the proceeds of the loans probably became deposits in country banks.

BAIRD thinks that the banks in country towns will probably hold deposits for at least a year or so until the deposits move to Detroit and to cities manufacturing automobiles, tractors and other equipment.

WIGGINS believes that the country banks are being swollen with deposits they will not retain.

TRAPHAGEN. Perhaps the floor under agricultural prices may help maintain farm income and deposits in country banks.

MODIFICATION OF REGULATION "W".

E. E. BROWN asks Traphagen to comment on this subject.

TRAPHAGEN states that this item and the following two items on the agenda were proposed by Allan Sproul. There are a number of bankers who have indicated that they believe the regulation is extremely difficult, if not impossible, to enforce, and that it might be desirable for the Board to give some consideration to changes which would make enforcement easier.

SPENCER states that some persons with whom he spoke regarding the regulation like it because it helps them with their collections.

E. E. BROWN reports that in general the big finance companies were originally for Regulation "W". However, now they would like to do away with the regulation. The furniture dealers apparently are divided on the question.

TRAPHAGEN. Sproul felt some changes could be made which would make the regulation easier to enforce.

E. E. BROWN. The Council recognizes that the matter of relaxing the regulation is partly a question of timing. It depends on how goods come to the market. As shortages disappear in the market, the control of items no longer short should be eliminated.

E. E. BROWN does not believe that Regulation "W" and the controls associated with it should become a permanent part of our economy.

BAIRD understands that the Federal Reserve Bank of the Ninth District served notice on the Board of Governors that the bank did not intend to enforce Regulation "W". The large banks and finance companies generally comply with the regulation but there are many others who violate it.

MCCOY thinks the Council should recommend doing away with Regulation "W".

WIGGINS believes a start in that direction should be made. He thinks that the Board should take steps now to do away with the regulation. Soft goods are going to come to the market in large supply, possibly before Christmas. The cotton mill warehouses are filled.

TRAPHAGEN. There are probably two sides to the question. If there is a large amount of consumer credit out when the next depression begins, it may make the depression more severe.

E. E. BROWN suggests stating to the Board that the Council believes the controls should be eliminated on all but a few items, one of the exceptions being automobiles. Country banks are finding it very difficult to enforce and it is resulting in widespread dishonesty. Brown asks the opinion of the Council, and all members are in agreement with the viewpoint he has expressed.

WIGGINS states that this regulation was a war measure and was not intended to help police collections in good times.

E. E. BROWN is not willing to have the Board of Governors given this authority as a permanent part of our economy.

PENICK asks whether abolishing the regulation will result in banks losing consumer paper to the finance companies.

E. E. BROWN reports that the finance companies are complaining that the banks are taking the best of the business and are leaving the poorest part to them.

WIGGINS believes that if we are in favor of a competitive economy, we must recommend eliminating the controls.

WHETHER OR NOT IT IS DESIRABLE TO MAKE RECOMMENDATIONS TO CONGRESS FOR CHANGES IN BANKING LAWS BY MEANS OF A SPECIAL REPORT EMBODYING THE JOINT RECOMMENDATIONS OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, THE PRESIDENTS OF THE FEDERAL RESERVE BANKS AND THE FEDERAL ADVISORY COUNCIL AS WAS DONE IN JANUARY, 1941, RATHER THAN CONFINING THESE RECOMMENDATIONS TO THE ANNUAL REPORT OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM.

E. E. BROWN asks Traphagen to comment on this item.

TRAPHAGEN states that Sproul submitted the question. It was Sproul's feeling that bankers would get further with Congress if the Board of Governors, the presidents of the Federal Reserve banks, and the Federal Advisory Council jointly submitted recommendations for changes in the banking laws, rather than merely to have recommendations submitted by the Board of Governors in its annual report.

E. E. BROWN believes it would be unwise to make this recommendation. The joint report to which Sproul referred as an illustration of the procedure to follow was closely related to the war situation at the time. Everything was subordinated to the war emergency. Brown objects to the proposal because the presidents of the Federal Reserve banks tend to be under pressure of the Board of Governors which fixes the salaries of the presidents. He calls attention to the fact that Sproul favored the Board's proposal that banks should be required to hold a certain percentage of their deposits in short-term government securities. Brown favors working with all the government agencies that are related to banking, such as the Treasury and Comptroller, and not only working with the Board of Governors and the presidents of the Federal Reserve banks.

J. T. BROWN asks whether it would ever be possible to get an agreement between the Board of Governors, the presidents of the Federal Reserve banks, and the Federal Advisory Council on changes in banking laws.

SPENCER thinks there would be a minority report of the Council attached to each report.

E. E. BROWN. The Council is apparently in agreement that this is not a workable proposal.

THERE ARE STILL A SUBSTANTIAL NUMBER OF BANKS IN THE COUNTRY WHOSE PREFERRED STOCK OR CAPITAL DEBENTURES ARE HELD BY THE RFC. SINCE IT SEEMS UNDESIRABLE FOR THE GOVERNMENT TO BE IN THE POSITION OF PERMANENTLY ADVANCING CAPITAL FOR THE BANKING BUSINESS AND SINCE THE PERIOD OF RECOVERY FROM WRITE-OFFS IS PRETTY MUCH A THING OF THE PAST, IT WOULD APPEAR DESIRABLE THAT SOME PLAN BE DEVELOPED WITH THE RFC WHEREBY THEIR HOLDINGS IN THESE BANKS COULD BE TRANSFERRED TO LOCAL OWNERSHIP.

E. E. BROWN asks Traphagen to comment regarding this subject.

TRAPHAGEN reports that Sproul feels the period of recovery from write-offs is largely past, and that something should be done to get the government capital out of the banks.

MCCOY states that he had charge of arranging for banks in Ohio to take RFC capital in the 1930's. In this capacity he recapitalized 91 per cent of the state banks of Ohio and many national banks. The banks were told that they could pay off the RFC at their convenience. Out of \$28 million of RFC capital now outstanding in Ohio banks, \$24 million is in two banks; only \$4 million is left in sixty-seven banks. The FDIC and the Board of Governors will not let some banks retire their RFC capital, because these agencies insist that the banks should maintain a 10 per cent capital ratio.

E. E. BROWN comments that perhaps the Board of Governors could place some publicity in the Federal Reserve Bulletin and possibly in other banking publications, which would encourage banks to pay off their RFC capital.

J. T. BROWN. In Mississippi many banks have set up 100 per cent reserves against their preferred stock. The reserves in Mississippi are subject to taxes ranging from 5 to 7 per cent. The FDIC prevents the banks in that state from transferring their reserves to surplus and eliminating the preferred stock. Brown states that the tax laws in his state have made the retirement of RFC capital very difficult.

E. E. BROWN. Perhaps the Council should recommend to the Board that it use its influence with the FDIC to encourage banks to retire the RFC capital.

MCCOY thinks the Board of Governors could be helpful to the member banks on this matter.

E. E. BROWN thinks the Board can ask its examiners to persuade banks to retire their RFC capital.

100 PER CENT CASH MARGIN REQUIREMENTS FOR THE PURCHASE OF LISTED SECURITIES

E. E. BROWN asks whether the Council wishes to request the Board to modify the present 100 per cent margin requirement. He points out that the stock market decline has been a healthy factor. However, if it should go too far, it may cause a rather serious deflation. He believes banks should be allowed to extend credit on stock market operations, and perhaps the time has come to change this requirement. There is another aspect of this question which is important. The A. T. & T. financing recently took the form of debentures because the stockholders could not borrow on stocks. It is important that owners of stocks be permitted to borrow on stocks in order to exercise their rights.

SPENCER believes as Brown does that the Board should give consideration to modifying the present 100 per cent margin requirements.

It may not be desirable now to reduce from 100 per cent to as low as 50 per cent; perhaps 75 per cent is desirable. The requirement as it applies to persons who wish to borrow on stocks to exercise rights should be removed. Spencer advises making this recommendation to the Board.

TRAPHAGEN asks Brown whether he means the present requirement should be modified as it relates to brokers as well as to banks.

E. E. BROWN replies that the modification should apply to both groups.

PENICK points out some of the inconsistencies existing between the state laws in Arkansas and the Federal Reserve regulations.

E. E. BROWN asks Traphagen's opinion regarding modification of the 100 per cent margin requirement, in view of the fact that his bank is located in the city with the New York Stock Exchange.

TRAPHAGEN believes that the Federal Reserve Bank of New York probably does not think this is the time to change the margin requirements. However, he personally believes the less regulation we have, the better our economy operates. The government cannot regulate the conduct of individuals forever. He believes that security holders should have the right to borrow. They own property just as real estate holders own property, and they should have the right to borrow to buy stocks as well as the right to borrow to buy real estate.

E. E. BROWN states that the question is undoubtedly one of the proper timing. To modify the requirements now may be interpreted as an effort to bolster a declining market. On the other hand, if the margin requirements are modified in a period of a rising stock market, the critics may state that this action would further promote the boom. It is desirable for the Board to consider whether the present time is the proper time to modify the margin requirements to 75 per cent, or perhaps 50 per cent. The Council is in agreement regarding the advisability of changing the present requirements in connection with persons who wish to borrow on stocks to exercise rights.

BAIRD. There never is a perfect time to change. The logical move seems to be to go to 75 per cent.

The meeting adjourned at 5:38 P. M.

On October 7, 1946, at 10:43 A. M., the Council held a joint meeting with the Board of Governors of the Federal Reserve System in the Board Room of the Federal Reserve Building.

All members of the Council were present except Mr. Winton.

The following members of the Board of Governors were present: Chairman Eccles; Vice Chairman Ransom (entered the meeting at 11:20 A. M.); Governors Draper, Evans, and Vardaman; also, Messrs. Thurston, Morrill, Paulger, Carpenter, Sherman, Vest, Thomas, Leonard, Smead, and Parry.

PROPOSED AMENDMENTS CONCERNING THE F.D.I.C. H.R. 7211 and S. 2494.

E. E. BROWN asks whether the Board of Governors has taken any position on the amendments. The Council is not in favor of taking any action at least until Congress meets again.

ECCLES. The Board has done nothing about the proposed amendments. The Board was not asked for its opinion, but it will undoubtedly give an opinion when it is asked. Eccles believes that the return of the money to the Federal Reserve Banks now would be a mistake. The problem of the Federal Reserve banks is to justify the large earnings they are making at present. He believes the bankers would be in a better position if they maintained the 1/12th of 1 per cent assessment even if it seems too large. He believes the banks are in a poor position when they argue against government subsidies in other aspects of the government's operations if they, at the same time, use government money in the F. D. I. C. He thinks the bankers will be in a better position if they pay off the government money, and he believes bankers should support the amendments.

E. E. BROWN states that the Council will take no action in view of the fact that the matter will not come up at least until the next Congress. He mentions that Harl has proposed that the fund be brought to \$1 billion and that thereafter the assessment should vary to keep the fund at this figure. The result would be that in good times there might be no assessments and in periods of depression and low earnings the assessments might be high.

AT PRESENT THE FEDERAL RESERVE BANKS BUY TREASURY BILLS IN OPEN MARKET THROUGH BROKERS. THIS IS A SOMEWHAT FICTITIOUS TRANSACTION BECAUSE ACTUALLY THERE ARE NO OTHER BIDDERS FOR MOST OF THE BILLS BOUGHT. IT HAS BEEN SUGGESTED THAT THE FEDERAL RESERVE BANKS, UNDER AN ARRANGEMENT WITH THE TREASURY, CONVERT THEIR BILL HOLDINGS INTO A SINGLE PIECE OF PAPER THAT WOULD NOT REQUIRE WEEKLY BUYING AND LIQUIDATION. HOWEVER, THIS MIGHT BE CONSTRUED AS DIRECT BORROWING BY THE TREASURY FROM THE FEDERAL RESERVE BANKS. IT SEEMS DESIRABLE THAT THE MECHANICS OF RESERVE BANK BUYING OF TREASURY BILLS SHOULD BE REVISED. THE QUESTION IS WHAT IS THE BEST PLAN TO USE.

E. E. BROWN asks whether the Board has given any further thought to the present plan of handling Treasury bills. The Council believes that the present plan, even if it is a somewhat fictitious transaction, is better than direct borrowing by the Treasury from the Federal Reserve banks.

ECCLES reports that the subject is still under study. The Board does not like the present plan. It was a war-time measure. The bills were permitted to increase in about the same volume as the expansion in the currency; as a result, the bills expanded to about \$17 billion. The bills were issued largely to meet the expansion of currency during the war. The bills also give banks ready access to the Federal Reserve banks. With only \$2 billion of the \$17 billion in bills held outside the Federal Reserve banks, the present arrangement should be changed. The Canadians hold about \$1 billion of the \$2 billion in bills outside of the Federal Reserve banks. All of the banks of the United States only hold about \$600 to \$700 million of these bills, and the bill is no longer a money market instrument. What is really going on is a deception and it is actually direct borrowing. Eccles believes the 7/8 per cent certificates will have to be supported because of the large amount of debt which is maturing from month to month. The banks will buy certificates because of the market support. The open market committee is now considering this whole problem. So long as the Treasury keeps up its retirement program, the banks will probably do little switching. The Board thinks that the government bond market will maintain its present degree of stability for the immediate future. So long as there is a 3/8 per cent bill rate, it tends to keep rates down. Eccles hopes after the first of the year to work out this matter with the Treasury.

E. E. BROWN states that the Council does not like either the present fictitious arrangement or a direct sale by the Treasury to the Federal Reserve banks. However, the present arrangement is preferable to a direct sale.

SPENCER asks what the rate would be on the \$5 billion if the Treasury borrowed direct.

ECCLES states that the Federal Reserve banks would fix the rate by negotiation with the Treasury. The Treasury has had occasional small over-drafts on which the rate has been 1/4 of 1 per cent. Eccles points out that for 22 years there was no prohibition against direct borrowing by the Treasury from the Federal Reserve banks.

WIGGINS believes the prohibition of direct borrowing is psychologically a good thing.

THE PRESENT STATUS OF THE GOVERNMENT BOND MARKET AND PLANS WHICH THE TREASURY MAY HAVE WITH RESPECT TO THE CONTINUATION OF DEBT RETIREMENT AND REFUNDING OF MATURING OBLIGATIONS.

E. E. BROWN states that this subject has already been partially discussed in connection with the previous item on the agenda. He asks whether there is any indication that the Treasury will stop its present program of retiring government obligations or whether it will continue its retirement program until the Treasury balances decline to about \$3 to \$5 billion.

ECCLES reports that he has not discussed the matter with the Treasury since his return from the West. He says that Morgenthau and his associates always felt more comfortable with a large cash balance. Eccles states that even though there is a bookkeeping deficit for the rest of the year, there will actually be a cash surplus. He is inclined to believe that the Treasury staff thinks it can get along with small balances and will continue to retire debt. For the balance of the calendar year, Eccles believes the following obligations will be retired:

\$1½ to 2 billion of November Certificates
\$500 million to 1 billion of December 1 Certificates
\$3.2 billion of 1-1/2 per cent notes due December 15

The foregoing figures indicate that approximately \$2 billion in certificates and \$3.2 billion in notes may be retired by the end of the calendar year if the Treasury permits cash balances to decline to approximately \$1½ or \$2 billion. The Treasury asks for the viewpoint of the Board on these matters, and these two agencies are generally in agreement. For the first three months of the next calendar year, Eccles anticipates that it may be possible to retire about \$4 billion of the debt. About one-half of the funds to retire this debt will come from the excess of the sales of E, F, and G bonds over the redemptions, and half will come from the excess of government cash income over the cash outgo. Eccles further reports that no support was given recently in the market to any government bonds.

E. E. BROWN states that banks in the large centers are being offered loans in substantial amounts. He gives three reasons for the increasing demand for bank loans: (1) A higher price level which results in a greater cost for inventories and in larger receivables; (2) increasing inventories due to strikes, partially manufactured goods, freight embargoes, car shortages, and O. P. A. regulations; and (3) companies with expansion programs had expected to finance these programs by selling stock, but the stock market decline has made it necessary for these companies to go to banks for loans. Money is tighter now than it has been for several years.

ECCLES states that although there has been an increase in the loans of commercial banks, there has been an over-all decrease of \$8 billion in deposits because of the government bond retirement program

MODIFICATION OF REGULATION "W"

E. E. BROWN states the Council believes that the regulations covering most items should now be eliminated. He mentions that Ransom had indicated some months ago that the restrictions would gradually be relaxed and finally eliminated as goods came into the market in adequate supply. Brown states that articles such as small radios are rapidly coming into the markets in sufficient quantities. There is wide-spread dishonesty in the enforcement of the regulation.

RANSOM asks whether Brown's statement is in the form of a recommendation by the Council.

E. E. BROWN replies that it is a recommendation of the Council.

RANSOM reports that the volume of consumer credit has increased in the last month.

WARDAMAN asks why consumer credit has increased in the last month.

PARRY reports that the following four factors accounted in large part for the increase:

(1) an increased supply of goods for sale; (2) higher prices; (3) promotional efforts of stores to increase their charge accounts; and (4) the rate at which people are paying off their charge accounts has slowed down.

ECCLES. If consumer credit continues to expand, it may go as high as \$20 billion. It will increase the inflation, and it will be a factor in helping to continue a boom. However, it may later bring a real collapse. The expansion of private credit in an inflationary period is just as bad as the expansion of government debt.

E. E. BROWN states again that Ransom, who was presumably speaking for the Board, indicated some time ago that it was planned to drop some of the controls of Regulation "W" as soon as goods came into adequate supply, but the controls have not been relaxed as anticipated. The Council believes some goods are already available in sufficient quantities so that the controls can be dropped.

RANSOM says that the Board is trying to take the necessary steps to eliminate some of the controls. However, he adds, some of the trades like the regulation.

WIGGINS replies that the regulation was not intended originally to be of assistance to the trades.

ECCLES states that the Board could ask the President to repeal the regulations. He does not believe it is practical to do away with a part of the regulation. If there is any change, he thinks that the regulation must be repealed in its entirety, and that it is not practical to keep control over only a few items.

VARDAMAN comments that if it is a matter of the repeal of all or the repeal of nothing, he favors eliminating all controls.

MCCOY asks how far the Board thinks it actually has control of the situation.

ECCLES replies that it is impossible to measure the extent to which the control has been effective, but he believes it has been reasonably effective. Eccles also states that if you repeal the regulation and have 10,000 banks soliciting consumer paper, consumer loans could go to \$20 billion. The regulation does at least maintain the steady liquidation of this type of credit, and even though new loans are made, old ones are being liquidated.

THOMAS. That is the important fact. Although new consumer credit is being extended, the regulation requires credit already outstanding to be paid off steadily. There is constant liquidation.

VARDAMAN states that the regulation stems from a Presidential order. He thinks it might be possible to suggest to the President that the President give notice to Congress that he expects to repeal the authority of the Board under the regulation. This might hasten the end of the regulation.

ECCLES says that Congress must finally decide whether this type of regulation is to be part of our permanent economy.

VARDAMAN asks whether it is not possible to release some articles like small radios from the control.

DRAPER doubts if this is practical.

E. E. BROWN states that he does not believe the Board realizes the extent to which the regulation is being violated. Many items that are unimportant dollar-wise could be eliminated.

BAIRD believes it would be possible to do away with the regulation as it applies to some items. He thinks it should be retained on automobiles.

WIGGINS reports that some persons may have to sell their government obligations if they cannot get consumer credit.

ECCLES thinks it is wiser to sell a government bond carrying a low rate rather than to borrow at a high rate on consumer credit. He states it is bad for the person of small means to borrow too much.

MCCOY comments that small loans worked out well in the 1920's and in the depression beginning in 1929.

WHETHER OR NOT IT IS DESIRABLE TO MAKE RECOMMENDATIONS TO CONGRESS FOR CHANGES IN BANKING LAWS BY MEANS OF A SPECIAL REPORT EMBODYING THE JOINT RECOMMENDATIONS OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, THE PRESIDENTS OF THE FEDERAL RESERVE BANKS AND THE FEDERAL ADVISORY COUNCIL AS WAS DONE IN JANUARY 1941, RATHER THAN CONFINING THESE RECOMMENDATIONS TO THE ANNUAL REPORT OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM.

E. E. BROWN states that the Council has discussed this matter and does not believe it is workable or practical. He does not believe the Board or the Council would find any advantage in a discussion of it.

ECCLES offers no objection.

THERE ARE STILL A SUBSTANTIAL NUMBER OF BANKS IN THE COUNTRY WHOSE PREFERRED STOCK OR CAPITAL DEBENTURES ARE HELD BY THE RFC. SINCE IT SEEMS UNDESIRABLE FOR THE GOVERNMENT TO BE IN THE POSITION OF PERMANENTLY ADVANCING CAPITAL FOR THE BANKING BUSINESS AND SINCE THE PERIOD OF RECOVERY FROM WRITE-OFFS IS PRETTY MUCH A THING OF THE PAST IT WOULD APPEAR DESIRABLE THAT SOME PLAN BE DEVELOPED WITH THE RFC WHEREBY THEIR HOLDINGS IN THESE BANKS COULD BE TRANSFERRED TO LOCAL OWNERSHIP.

E. E. BROWN states that there has apparently been some objection by the F.D.I.C. examiners to the retirement of RFC capital. The objection is said to be that the capital ratio in some banks would be too low after the retirement of the RFC capital. In other instances, the tax laws of states make it difficult for banks to retire the RFC capital. The Board of Governors might be helpful by asking its examiners to encourage banks to pay off their RFC capital. The period of recovery from write-offs is largely a matter of the past and it would seem desirable to suggest that banks retire this capital.

ECCLES doubts whether the Board should "get in the middle" on this matter. The RFC has a contract with each bank which took RFC capital. A bank may easily say that the retirement of the RFC capital is of no concern to the Board of Governors so long as the bank fully meets its contract and its stockholders and depositors are entirely satisfied. The RFC capital is to be retired out of earnings and so long as a bank is complying with its contract, the Board is hardly in a position to insist that the RFC capital be retired now. If the RFC capital were being increased, then the Board might be in a position to object.

E. E. BROWN states that there have been some reports that the examiners of the Federal Reserve System have objected to the retirement of RFC capital.

ECCLES replies that the examiners of the Federal Reserve System have objected only where the retirement of the RFC capital would leave a bank with inadequate capital.

VARDAMAN states that several groups have come to him and asked that the Board do something about encouraging the retirement of RFC capital. Vardaman does not wish in any way to interfere in the management of any bank's affairs so long as it is operating properly and is abiding by a contract it may have with the RFC. He states that the next Congress may move to make private corporations pay off government funds which they are using. He reports also that those in charge of state bank examinations definitely expect to take steps to encourage the payment of RFC capital, and Cyril Upham of the Comptroller's Office also indicated that they favor the retirement of this capital.

E. E. BROWN states that another problem in this connection is presented when stock of a bank is held in its trust department. When the bank proposes to issue new common stock to retire RFC capital, Regulation "F" has prevented the bank's trust department from taking its share of the new stock. He suggests a modification of Regulation "F" to take care of this situation. He again stresses the fact that banks should be encouraged to retire their RFC capital.

ECCLES indicates that the Board will give consideration to the problem raised in connection with Regulation "F" and the inability of trust departments to take down their share of new stock in connection with stock held in their trust departments.

100 PER CENT MARGIN REQUIREMENTS FOR PURCHASING LISTED SECURITIES

E. E. BROWN asks whether the Board has given any consideration to the desirability of changing these requirements.

ECCLES replies that the Board expects to discuss this matter in the immediate future and is not in a position to go into the matter fully now. He states that the presidents of the Federal Reserve banks advised against making any change now.

E. E. BROWN believes the question is, in a large measure, one of timing. To change the margin requirements to 75 per cent or 50 per cent now might lead critics to say that an effort was being made to stop a declining market. On the other hand, if the requirements are modified on a rising stock market, the critics will say that the modification of the requirements further increases speculation.

ECCLES thinks the stock market has been made more stable in re-

dent months by the absence of borrowing for speculation.

E. E. BROWN reports the Council believes the situation has undergone a considerable change in the last ninety days. The Council is not fixed in its judgment as to whether the margin requirements should be modified to 75 per cent or 50 per cent. However, there is one aspect of the question on which the Council is agreed, and that is that something should be done now to enable owners of stocks to borrow for the purpose of exercising rights. The owners of stocks now cannot borrow on stocks to exercise their rights. In some cases, they are even borrowing on an unsecured basis. They should be allowed to borrow to exercise their rights.

DRAPER hopes this can be worked out. It has been discussed at the President's Conference.

VARDAMAN comments that there are obviously two propositions: (1) borrowing to buy stocks; and (2) borrowing to exercise rights.

E. E. BROWN states that a person should have the right to borrow on stocks. He calls attention to the fact that the A. T. & T. issued debentures in order to obtain the funds for the necessary expansion of the Company's facilities.

ECCLES thinks it might be better in the long run if some of the present expansion projects were deferred because of the exorbitant prices. The stock market has declined, but the labor situation is still tight and shortages persist. Some actual decline in the economy may be desirable.

VARDAMAN says everything is high but the cost of money. Many companies are borrowing now at low rates in order to have the funds available to expand their operations at a later date.

ECCLES believes the 100 per cent margin requirement probably kept the market from going even higher. The market has been flooded with a large number of small, undigested issues. Corporations have been floating 30 to 40 year issues at 2-1/2 per cent and the banks have been making term loans at 1-3/4 per cent. The present decline has been a benefit to our economy.

REVISED BANK HOLDING COMPANY BILL

E. E. BROWN asks whether the Board has further discussed the Revised Bank Holding Company Bill.

ECCLES reports there has been no further discussion of the bill. Eccles states that the Board could not get the Treasury, Comptroller, and the F. D. I. C. all to agree on a bill. Consequently, the Board worked out a bill and placed it in the legislative hopper. The Board expects to bring up the bill with Congress after the first of the year.

The meeting adjourned at 1:20 P. M.

The Council reconvened in the Board Room of the Federal Reserve Building at 2:10 P. M. on October 7, 1946, to hear Dr. Woodlief Thomas, Director, Division of Research and Statistics of the Federal Reserve System.

All members of the Council were present except Mr. Ed. H. Winton.

E. E. BROWN introduces Thomas who speaks on "Latin-American Trends". (Dr. Thomas has provided a complete mimeographed statement of his comments which is attached).

* * * *

E. E. BROWN asks how long the Latin-American countries will continue to demand American goods. At present they seem to be short of many of the same goods which are scarce here.

THOMAS replies that the Latin-American countries are not so short of consumer goods, but they are short of building supplies and hard goods. They are worried about their ability to buy here in the future. Consequently, they are interested in obtaining loans from us now.

PENICK comments that the man in the street must have a serious living problem in view of the inflation that exists in some of these countries.

THOMAS replies that it is a serious problem. He states that it will take a long time to build up the living standards of the lower income groups.

BAIRD asks whether the management of the central banks changes as often as the governments of some Latin-American countries change.

THOMAS replies that the management of the central banks does not change as frequently as the governments change. There are generally men who are career officials in the banks who continue through various political administrations to manage the affairs of central banks.

The meeting adjourned at 3:22 P. M.

September 25, 1946

CONFIDENTIAL

REPORT ON MEXICO CITY CONFERENCE OF CENTRAL BANK EXPERTS

by

DAVID L. GROVE

For the past few years, there has been considerable informal discussion among the central banks of the Western Hemisphere concerning the desirability of holding a conference at which technical experts of these institutions would meet to exchange informal views about the monetary and banking problems of their respective countries and of the Hemisphere as a whole. The outcome of these discussions was that the Bank of Mexico convoked a conference, which was held in Mexico City between August 15 and 30. With the exception of Honduras, Panama, Cuba, and Haiti, all of the 21 republics of the Western Hemisphere were represented. The absence of Cuba was due to the fact that it does not yet have a central bank or its equivalent.^{1/}

With the exception of a decision to establish a Permanent Committee, the conference passed no resolutions and arrived at no official conclusions. The conference was called for the purpose of providing an opportunity for informal discussions which would in no way commit or embarrass the organizations which the delegates represented. It was attended by no publicity. It was the feeling of apparently all of the delegates that they profited from this interchange of ideas and that the associations established would pave the way for greater cooperation among the participating central banks than has existed heretofore.

The program of the conference was organized around the deliberations of three committees:

- I. A Committee on Monetary and Credit Controls.
- II. A Committee on Balance of Payments and Foreign Exchange Problems.
- III. A Committee on Cooperation among Research Departments of Central Banks.

^{1/} The United States delegation consisted of Mr. Woodlief Thomas and Mr. David Grove of the Federal Reserve Board, Mr. Horace Sanford and Mr. Henry Wallich of the Federal Reserve Bank of New York, and Mr. Watrous Irons of the Federal Reserve Bank of Dallas. The International Monetary Fund was represented by Mr. Robert Triffin and Filipe Pazos.

This third committee, in turn, was split into six subcommittees:

- A. Functions of Economic Research Departments.
- B. Monetary and Banking Statistics.
- C. National Income.
- D. Balance of Payments.
- E. Other Statistics.
- F. Interchange of Statistics and Personnel.

The delegates participated in the committees or subcommittees which were of interest to them, and meetings were scheduled in such a way as to present as little conflict as possible.

Too much space would be required to review all of the discussions which took place and the documents which were presented during the course of the Conference. Accordingly, an endeavor will be made to cover only some of the highlights.

Committee I, the Chairman and Vice-Chairman of which were Mr. Thomas of the Federal Reserve Board and Mr. Triffin of the Monetary Fund, respectively, first reviewed recent monetary and banking developments in the various countries. Emphasis in nearly all cases was placed on the development of inflationary forces. There was a general opinion among the Latin Americans that the inflation in their countries is the result of the highly favorable balances of payments which they have experienced during the war, and that rather little can successfully be done to counteract inflation until imports from the United States become available in larger amounts. It was pointed out by Mr. Thomas that while our exports help combat inflation in the recipient countries, they have the contrary effect here at home, and for this reason the United States has found it necessary to place certain restrictions on exports, and will have to continue to do so.

The theory that the economies of the Latin American countries move more or less automatically in response to developments in the United States appeared to be shared by all of the Latin American delegates, but was most eloquently expounded by Dr. Prebisch, formerly manager of the Central Bank of Argentina. He distinguished between "central" and "peripheral" countries. An exact definition of a "central" country was not made; however, certain characteristics of central countries were indicated. First of all, a central country must be one which plays a large role in world trade. Secondly, it must be one which, in times of depression, can produce a large and rapid capital inflow, either through repatriation of its own capital investments abroad or through attraction of foreign capital. There was the implication that there can be only one central country at a time, with other countries being either quasi-central or peripheral. Until recently, England was the central country, but its position has now been taken by the United States.

Dr. Prebisch's thesis is that the control of booms and depressions rests with the central and quasi-central countries, and that the peripheral countries can do relatively little to combat cyclical movements, although he admitted that unsound domestic policies of the peripheral countries could aggravate the situation. Mr. Triffin pointed out that

depressions are not always transmitted from the central countries, as witness the depression in some of the agricultural countries in the late 'twenties, when income in the central countries was still high. These depressions were caused by overproduction in the agricultural countries and not by a decline in the demand of the central countries.

After the rather rapid review of recent developments in each of the countries, there followed a lengthy discussion of recent central bank policies and of the instruments of control adopted to carry out these policies. Opinions were exchanged with respect to the use of rediscounts and advances, open-market operations, flexible reserve requirements, selective credit controls, capital requirements, and interest rates as instruments of control, and the experiences of the various countries with these instruments were described. The Latin Americans were unanimous in expressing the view that the traditional instruments of control cannot always be adapted to the conditions prevailing in their countries and that where an attempt has been made to do so, their use has been ineffective. The lack of a government securities market limits the use of open-market operations, considered one of the most potent monetary weapons here in the United States. Changes in reserve requirements are relatively ineffective because the favorable balances of payments during the war period have increased bank reserves tremendously. In many of the countries, the increase in the money supply has been largely due to the acquisition of international reserves, and not to an expansion of bank credit. In these cases, increases in reserve requirements would have little effect. As a case in point, the Mexican delegates remarked that, for banks located in the Federal District of Mexico, reserve requirements against demand deposits were raised to a level of 50 per cent, but the inflow of foreign exchange constantly created new bank reserves and made possible further credit expansion. On May 22, 1944, the Bank of Mexico placed a ceiling on the loan and corporate security holdings of all banks, based, in each case, on the amounts of such assets held on May 17, 1944. The ceiling has proved to be effective in restricting the total volume of bank credit, but has presented many administrative problems. Furthermore, the method is not selective, and one of the results has been to produce a shift in the composition of bank assets; relatively more funds are going into types of loans which the Bank of Mexico wishes to discourage but on which the banks obtain a higher rate of return, and relatively less funds are available for operations such as production loans, which the Bank of Mexico wishes to encourage.

The prevailing rates of interest on bank loans are very high in Latin America. Mr. Villasenor, Director General of the Bank of Mexico, declared that the experience of the central banks has been that efforts to bring interest rates down are usually unsuccessful, and that in cases where they are successful, there is often an outflow of capital which makes the continuation of the effort impossible or at least unadvisable.

A great deal of attention was given to a discussion by Mr. Thomas of the measures of selective credit controls on security loans and consumer credit which have been adopted by the United States and to

his evaluation of the problems involved in applying such controls. The Latin American countries have adopted very few such controls, but some of them, notably Mexico, felt that if inflationary forces continue to mount, then similar measures may, in some cases, have to be adopted in their countries.

Committee II, which was designated to study balance of payments and foreign exchange problems, was presided over by Dr. Hermann Max, Chief of the Research Department of the Central Bank of Chile.

Balance of payments and foreign exchange problems are the central problems of most of the Latin American Countries. To a considerable extent, their economic activities are governed by changes in foreign demand for their exports, and they have little control over this demand. Exchange controls have thus come to assume a greater importance than domestic controls. Furthermore, domestic policies are often limited or counteracted by changes in the balance of payments.

Mr. Urquidi, of the Bank of Mexico, presented a paper entitled "Analysis and Characterization of Various Types of International Disequilibrium," in which he endeavored to classify disequilibria according to their origin, intensity, duration, and other characteristics. The problem of defining a "fundamental disequilibrium" was of special interest to all the delegates because of the importance of this concept in the Articles of Agreement of the International Monetary Fund.

Dr. Prebisch stated that fundamental disequilibrium should be defined in terms of cost-price relationships. A fundamental disequilibrium can come about in two ways: (1) if domestic costs of export goods rise and prices fail to follow, and (2) if export prices fall and costs fail to follow.

Mr. Triffin expressed the view that the definition of a fundamental disequilibrium cannot be made entirely dependent upon cost-price relationships. He then offered the following definition:

"A fundamental disequilibrium is a maladjustment in a country's economy so grave and persistent that the reestablishment or maintenance of a satisfactory level of employment, prices, economic activity, and national income would require extraordinary measures to defend the equilibrium in the exchange rate, the establishment of a permanent system of exchange control, a thorough revision of the tariff system, etc."

Both Mr. Triffin and Dr. Prebisch appeared to agree that, insofar as a disequilibrium of the balance of payments is concerned, exchange control is likely to be more effective, if properly established and administered, than is devaluation, at least for Latin American countries. The chief effect of devaluation in Latin America has been to raise domestic income and employment; in most cases any beneficial effects on the balance of payments have been negligible in the short run and their existence in the long run has been questionable. Dr. Max did not agree with this conclusion, however, and appeared to place much more faith in the efficacy of devaluation in remedying an unfavorable balance of payments.

Mr. Triffin explained that not all disequilibria in the balance

of payments are fundamental, and, consequently, not all disequilibria require corrective action. Furthermore, not all fundamental disequilibria manifest themselves in a disequilibrium in the balance of payments. It is most important to distinguish between the disequilibrium itself (or its causes) and its concrete manifestation in any given case. In accordance with the theory of general equilibrium, any disturbance in the economy of a country has repercussions and manifestations in various sectors. Thus, a disequilibrium which originates in external problems of international economic equilibrium may manifest itself not in a disequilibrium of the balance of payments, but in one which appears to be purely domestic, such as, for example, grave unemployment.

Once an agreement has been reached that a given disequilibrium is a fundamental one, it does not follow that a modification of the parity of the currency would constitute the only, or even the best, way of remedying the situation. He stated that the following points must be considered:

(1) What practical alternatives are at the disposition of the country or of the international community to remedy said disequilibrium? For example, exchange control might be advisable in the case of one country and inadvisable in the case of another.

(2) What will be the international repercussions of a change in parity?

Mr. Triffin said that he believes that other countries should not have the right to object to a modification of the parity of one country simply because the modification would result in a reduction in their own exports or in an increase in their imports. In many cases, a country which finds itself in a position of fundamental disequilibrium cannot remedy the situation except by increasing its exports and reducing its imports. The fact that a modification of the parity effectively leads to such a result should not be an objection against the adoption of this measure. As a general thesis it might be said that these consequences of a modification of parity should not be used as an objection in instances where the increase in exports and the decrease in imports simply result in the correction of the disequilibrium and not in an excessive accumulation of gold and foreign exchange. The effects on other countries should be carefully considered, of course, and in each case the problem should be examined to see if other measures might not be preferable, and if other measures should be adopted simultaneously.

The delegates attending the meetings of Committee II were very much interested in a discussion of the system of exchange control which Mr. Triffin has introduced in the legislation of Paraguay and Guatemala. Dr. Prebisch then related the experiences of the Central Bank of Argentina with a similar system, and explained why, in his opinion, exchange control must at times be adopted by the Latin American countries so long as the central countries continue to be subject to intense cyclical fluctuations.

Committee III, which was entitled "Cooperation among the Economic Research Departments," as has already been indicated, established six subcommittees, each of which studies one of the following problems:

(1) functions of economic research departments, (2) monetary and banking statistics, (3) calculation of national income, (4) balance of payments statistics, (5) other statistical data, and (6) interchange of information and personnel.

The Subcommittee studying monetary and banking statistics suggested:

(1) that all the central banks adopt uniform and comparable definitions and forms for the presentation of monetary and banking statistics;

(2) that the uniform data mentioned above be interchanged by all the central banks of the Western Hemisphere with one another.

The subcommittee proposed adoption of uniform central bank and commercial bank balance sheet forms which Mr. Triffin had submitted. These balance sheets, together with the total monetary issue of the Treasury, would supply all the data necessary for monetary analysis.

Two statistical methods of monetary analysis were presented, one by Mr. Triffin and another by Dr. Prebisch and Mr. Pratt, who is Chief of the Monetary and Banking Statistics Section of the Research Department of the Bank of Mexico. The basic difference between the two systems was that Mr. Triffin excluded Treasury deposits from the money supply whereas Dr. Prebisch and Mr. Pratt included them. The subcommittee decided that the central banks should experiment with both systems in order to see which one proves to be the more useful in practice.

The subcommittee studying national income suggested:

(1) that central banks promote or themselves undertake estimations of National Income, Net National Product, Gross National Product, Consumption, Savings, and Investment;

(2) that this work be initiated by estimating national income, using the payments approach, and then later, in order to check the results, that estimates be made of Gross and Net National Product using the Use-of-Product approach, and

(3) that every effort be made to see to it that the 1950 census includes all the elements necessary for the above-mentioned estimates.

The subcommittee studying balance of payments statistics recommended:

(1) that an effort be made to present balance of payments data in a comparable form;

(2) that the values be expressed both in national currency and in United States dollars;

(3) that estimates be made of the expected demand for and supply of foreign exchange for the use of the monetary authorities;

(4) that all international transactions be computed in order that the balance of payments register not only movements of foreign exchange or financial movements, but all transfers of economic values;

(5) that new domestic gold production, excluding domestic industrial consumption, be included among current transactions. The reason for this is that, since gold is considered as a liquid international asset, the purchases of domestic gold production by the central bank should be considered as a source of supply of international means of payment; and

(6) that the studies of balances of payments not be limited to a simple presentation of data, but that the procedures followed be explained and that an analysis be made of the effects of the various components of the balance of payments on other economic factors such as national income, money supply, price levels, etc.

The subcommittee studying other statistical data discussed the necessity of preparing adequate price, production, cost of living, and other statistical series and some of the technical problems involved in so doing.

The subcommittee charged with the discussion of interchanging information and personnel made one of the most important contributions of the Conference. It suggested the establishment of a Permanent Committee of Central Bank experts of the American Continent whose principal functions would be the following:

(1) To coordinate and promote interchange of

- (a) information about legislative and regulatory measures;
- (b) economic and statistical studies of a non-confidential character; and
- (c) bibliographical information;

all this to the extent that it affects or refers directly or indirectly to central banks.

(2) To facilitate and promote the interchange and training of technical personnel of the central banks in every way that may be considered adequate.

(3) To formulate a provisional agenda for a second conference of experts on central banking problems of the American Continent.

(4) To contribute, through the preceding functions, to the intensifying and broadening of studies on central banking in the American Continent and to propose the best form of permanently systematizing said studies.

It was proposed that this permanent committee consist of six

members, each appointed for a period of two years, who would, at the present time, represent the central banks of Chile and Argentina for South America; Colombia and Costa Rica for the Carribean and Central American area; and Mexico and the United States for North America. The committee would function through a permanent secretariat in that country. If any central bank does not accept its nomination as a member of the permanent committee or withdraws from said committee, the other members would designate another central bank to take its place. The permanent committee would begin functioning in a provisional manner upon the conclusion of the present conference and would assume a definitive character once the central banks on the committee have accepted their appointment.

Committee III approved the recommendation of its subcommittee and a resolution based thereon was approved by a plenary session of the Conference.

The Permanent Committee should provide a most useful means of giving continuity and permanence to the interchange of information and ideas which was so successfully initiated at the Mexico City Conference.

The representatives of the Central Bank of Chile requested that the second conference, which will be held about two years from now, take place in Chile.